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THE STATUS OF PROMISSORY NOTES UNDER THE SECURITIES ACT OF 1933 AND THE SECURITIES EXCHANGE ACT OF 1934

INTRODUCTION

The status of promissory notes as securities within the meaning of the Securities Act of 1933¹ and the Securities Exchange Act of 1934² is an oft-litigated question which has confounded both practitioners and academicians. Until recently, courts commonly adhered to the seemingly explicit definitional provisions of both statutes, finding almost all notes to be securities.³ Today, a literal construction of the statutory language defining security to include "any note"⁴ is viewed as impractical and unwarranted in light of the

¹ 15 U.S.C. §§ 77a-77aa (1970 & Supp. V 1975).

² 15 U.S.C. §§ 78a-78kk (1970 & Supp. V 1975).

³ See, e.g., *Lehigh Valley Trust Co. v. Central Nat'l Bank*, 409 F.2d 989 (5th Cir. 1969), wherein the court stated that the "definition of a security has been literally read by the judiciary to the extent that almost all notes are held to be securities." *Id.* at 991-92; *accord*, *Llanos v. United States*, 209 F.2d 852 (9th Cir. 1953); *Movielab, Inc. v. Berkey Photo, Inc.*, 321 F. Supp. 806 (S.D.N.Y. 1970), *aff'd per curiam*, 452 F.2d 662 (2d Cir. 1971); *SEC v. Addison*, 194 F. Supp. 709 (N.D. Tex. 1961).

⁴ Section 2(1) of the Securities Act of 1933, 15 U.S.C. § 77b(1) (1970) provides:

When used in this subchapter, unless the context otherwise requires—

(1) The term "security" means any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas or other mineral rights, or, in general, any interest or instrument commonly known as a "security," or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing.

The Securities Exchange Act of 1934 § 3(a)(10), 15 U.S.C. § 78c(a)(10) provides in part:

(a) When used in this chapter, unless the context otherwise requires—

. . . .

(10) The term "security" means any note . . . but shall not include currency or any note, draft, bill of exchange, or banker's acceptance, which has a maturity at the time of issuance of not exceeding nine months, exclusive of days of grace, or any renewal thereof the maturity of which is likewise limited.

It should be noted that while the definitional provisions of the 1933 and 1934 Acts vary slightly, they are considered identical for antifraud purposes. See *Tcherepnin v. Knight*, 389 U.S. 332, 335-36 (1967).

Individuals incurring financial losses and alleging fraud on the part of promoters or issuers of various instruments often seek relief under the securities acts in the federal courts. Where the sole basis of jurisdiction is the existence of a transaction involving a security, the court must, as a threshold determination, decide whether the particular instrument is a security. See *Beury v. Beury*, 127 F. Supp. 786 (S.D.W. Va. 1954) wherein the court observed that "[t]o bring an action for damages [under the antifraud provisions] within the jurisdic-

primary goals and policies underlying the federal securities legislation.⁵ In attempting to depart from the earlier literal view, many courts have relied upon the definitional preambles of the Acts, which extend the scope of the definitions throughout the statutes "unless the context otherwise requires."⁶ Pursuant to this latter phrase, the courts have sought to effectuate the presumed intent of Congress by examining carefully the context in which a promissory note is exchanged to determine whether the noteholder is entitled to the protection of federal securities law.⁷ Predictably, because of the lack of express congressional direction in the matter, courts have differed in their analyses of these transactions, and various approaches have evolved to determine whether a given note falls within the definition of a security.⁸

tion of a federal court on other than diversity grounds, the action must be one to enforce some liability or duty created by the Securities Exchange Act of 1934" *Id.* at 789. The plaintiffs in *Beury* failed to allege conduct which violated a duty under the Act. Analogous to a failure to allege actionable conduct is the allegation of conduct which otherwise would have been actionable had the instrument properly been classified a security. *Cf. ITT v. Vencap, Ltd.*, 519 F.2d 1001 (2d Cir. 1975) (manufacture of fraudulent securities in the United States for export sufficient to sustain subject matter jurisdiction). With the demise of the literalist view, see notes 11-26 and accompanying text *infra*, the importance of a relatively uniform standard, one that injects a greater degree of predictability for making this determination, has become increasingly apparent. See Note, *Bank Loans as Securities*, 51 ST. JOHN'S L. REV. 440, 441 (1977). See generally Long, *Introduction, Interpreting the Statutory Definition of a Security: Some Pragmatic Considerations*, 6 ST. MARY'S L.J. 96 (1974); Pollock, *Notes Issued in Syndicated Loans—A New Test to Define Securities*, 32 BUS. LAW. 537 (1977) [hereinafter cited as Pollock].

⁵ An examination of the legislative history of the 1933 and 1934 Acts reveals that Congress intended only investment transactions to be included within the statutory coverage. See notes 16-22 and accompanying text *infra*. In recognition of this fact, courts have utilized the doctrine of "equitable interpretation" to restrict the literal expression of the statute according to the spirit and policy of the legislation. See notes 27-65 and accompanying text *infra*. See generally 2A J. SUTHERLAND, *STATUTES AND STATUTORY CONSTRUCTION* § 54.03 (4th ed. 1973) [hereinafter cited as SUTHERLAND].

⁶ Securities Act of 1933, § 2(1), 15 U.S.C. § 77b(1) (1970); Securities Exchange Act of 1934, § 3(a)(10), 15 U.S.C. § 78c(a)(10) (1970). Many courts which have rejected the literal approach have relied upon this language. See, e.g., *Exchange Nat'l Bank v. Touche Ross & Co.*, 544 F.2d 1126, 1131-38 (2d Cir. 1976); *Joseph v. Norman's Health Club, Inc.*, 336 F. Supp. 307 (E.D. Mo. 1971).

⁷ See, e.g., *Zabriskie v. Lewis*, 507 F.2d 546 (10th Cir. 1974) (promissory note given in exchange for loan, proceeds of which were used to promote a business venture, is a security); *Bellah v. First Nat'l Bank*, 495 F.2d 1109 (5th Cir. 1974) (six-month bank note is not a security); *Zeller v. Bogue Elec. Mfg. Corp.*, 476 F.2d 795 (2d Cir.), *cert. denied*, 414 U.S. 908 (1973) (demand note issued by parent corporation with term less than 9 months, collateralized with stock of subsidiary corporation, is a security). See generally Lipton & Katz, "Notes" *Are Not Always Securities*, 30 BUS. LAW. 763, 770-71 (1975).

⁸ Tests which have been employed by courts in determining the extent to which promissory notes are covered by the 1933 and 1934 Acts generally include the literalist approach, see notes 11-15 and accompanying text *infra*, and an "economic realities" or "context-over-

While certain fundamental principles are common to many of the judicially developed approaches,⁹ each technique has its own distinguishing features, areas of emphasis, and shortcomings.¹⁰ It is suggested that to most effectively implement a context-oriented method of analysis, criteria gleaned from a bulk of case law should be utilized collectively to identify those transactions which Congress intended to be within the purview of the 1933 and 1934 Acts. It is the purpose of this Note to discuss the treatment historically afforded promissory notes under the securities laws and, through examination of various authorities, to isolate those factors that hopefully may serve as the basis of a test which is flexible in application, yet which promotes predictability and uniformity of result.

THE DEMISE OF THE LITERAL APPROACH

The departure from a literal reading of the statutory definition of a security has occurred in part because of the wide range of transactions which may involve the transfer of a promissory note. Although promissory notes are basically written declarations in which individuals pledge to pay a specific amount of money at a specified time,¹¹ these unilateral instruments are drafted and exchanged in many different forms, in many dissimilar contexts, and

text" test under which an evaluation is made of the transaction underlying the issuance of the note. See notes 27-65 and accompanying text *infra*. See generally Pollock, *supra* note 4, at 539-50.

⁹ A significant amount of case law and commentary has dealt in depth with the general policy considerations underlying the federal securities laws. See *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180 (1963), wherein the Court described the fundamental purpose of all six major federal securities acts as the substitution of "a philosophy of full disclosure for [that] of *caveat emptor* [in order] to achieve a high standard of business ethics in the securities industry." *Id.* at 186. Embodied in this policy is the goal of both the 1933 and 1934 Acts of protecting the public, and particularly the investor, from fraudulent or speculative schemes of promoters. See, e.g., *SEC v. Glenn W. Turner Enterprises, Inc.*, 474 F.2d 476 (9th Cir.), *cert. denied*, 414 U.S. 821 (1973). See notes 27-65 and accompanying text *infra*.

¹⁰ The various courts of appeals do not all agree upon the factors which should be weighed in evaluating whether a particular item is a security. This divergence has led to the development of a number of tests, each of which reflects a particular court's view of the essential elements of a security transaction. As a result, similar situations may produce contradictory holdings in different courts as to the applicability of the federal securities laws. Compare *Exchange Nat'l Bank v. Touche Ross & Co.*, 544 F.2d 1126 (2d Cir. 1976), with *Great W. Bank & Trust v. Kotz*, 532 F.2d 1252 (9th Cir. 1976) (*per curiam*).

¹¹ Slight variations of the basic definition of a note have been articulated in judicial decisions. See, e.g., *Aetna Oil Co. v. Glenn*, 53 F. Supp. 961 (W.D. Ky. 1944); *Kirkland v. Bailey*, 115 Ga. App. 726, 155 S.E.2d 701 (1967). See generally Comment, *Notes as Securities Under the Securities Act of 1933 and the Securities Exchange Act of 1934*, 36 Md. L. Rev. 233, 236 n.13 (1976) [hereinafter cited as *Notes as Securities*].

among a wide variety of parties.¹² Most common among the various types of promissory notes are the following: instruments given by an individual in exchange for a loan, ranging from the simple I.O.U. to the sophisticated installment purchase agreement; "debt obligations"¹³ which are utilized by corporations and other enterprises for general financing purposes and constitute the foundation of the capital structure of many business entities; and short term unsecured promissory notes known collectively as "commercial paper."¹⁴ A literal construction of the definitional provisions of the 1933 and 1934 Acts would result in the inclusion of all promissory notes otherwise within the scope of the statutes without regard to the nature of the underlying transaction in which the notes are exchanged.¹⁵

¹² See generally Hammett, *Any Promissory Note: The Obscene Security—A Search for the Non-Commercial Investment*, 7 TEX. TECH. L. REV. 25 (1975) [hereinafter cited as Hammett].

¹³ Debt obligations often are utilized extensively while a corporation is in its organizational stages. For a brief discussion of the function of debt in corporate financing see W. CARY, *CASES AND MATERIALS ON CORPORATIONS* 115-17 (abr. 4th ed. 1970).

¹⁴ One early and often-cited definition of commercial paper includes within the meaning of that term "[b]ills of exchange, promissory notes, bank-checks, and other negotiable instruments for the payment of money, which, by their form and on their face, purport to be such instruments as are, by the law-merchant, recognized as falling under the designation of 'commercial paper.'" BLACK'S LAW DICTIONARY 338 (rev. 4th ed. 1968) (citation omitted). For an in depth examination of the functions of commercial paper in the securities area, see Hicks, *Commercial Paper: An Exempted Security Under Section 3(a)(3) of the Securities Act of 1933*, 24 U.C.L.A. L. REV. 227 (1976). The definitional provisions of the 1933 and 1934 Acts differ significantly with respect to commercial paper. Under the 1934 Act short-term notes are specifically excluded from the definition of a security, subject to the "unless the context otherwise requires" language. *Id.* at 228. See generally Schweitzer, *Commercial Paper and the Securities Act of 1933: A Role for Registration*, 63 GEO. L.J. 1245 (1975); Comment, *The Commercial Paper Market and the Securities Acts*, 39 U. CHI. L. REV. 362 (1972).

¹⁵ The number of transactions in the ordinary course of business which involve promissory notes is quite large. On a practical level, this fact militates in favor of an interpretation which limits the applicability of the securities laws to certain delineated types of notes and thus spares the already congested federal court calendars from inundation with 10b-5 claims arising from small private commercial transactions. One student commentator has stated that "one must question whether anything but the most unequivocal congressional mandate should dictate the introduction to the federal courts of a substantial class of cases traditionally tried in state forums." Comment, *The Status of the Promissory Note Under the Federal Securities Laws*, 1975 ARIZ. ST. L.J. 175, 182. See *Lino v. City Investing Co.*, 487 F.2d 689 (3d Cir. 1973). The *Lino* court pointed out that "[t]o accept [the literal] argument would mean that any consumer who bought an article 'on time' and issued a note would be able to sue in a federal court on the theory that the retailer had purchased his 'security.'" *Id.* at 695. *Accord*, *Movielab, Inc. v. Berkey Photo, Inc.*, 321 F. Supp. 806 (S.D.N.Y. 1970), wherein the court noted that under a literal construction of the definitional provision, "jurisdiction could be invoked with respect to any claim of fraud in connection with the issuance of a check or note, no matter how small the transaction (e.g., the purchase of an automobile or refrigerator), provided the mails or some other instrumentality of interstate commerce were used" *Id.* at 808.

When viewed against the backdrop of the legislative history of the 1933 and 1934 Acts, as well as the intended regulatory and remedial benefits of the legislation, this literal approach appears unjustified.¹⁶ The primary purpose behind the 1933 and 1934 Acts was to protect the *investing* public from the types of abuses and unfair practices which preceded the economic depression of the late 1920's.¹⁷ The Supreme Court has observed that securities legislation was enacted to eliminate abuses in a previously unregulated market and that the intended focus of the legislation was upon securities sold to raise capital for profitmaking purposes.¹⁸ Thus, according to the Court, Congress intended the application of the Acts to hinge upon the "economic realities" of the underlying transactions and directed the thrust of the statutes toward the prevention of fraud and the protection of investors.¹⁹ This interpretation is supported by congressional reports accompanying the 1933 and 1934 Acts wherein continual emphasis was placed on the Acts' coverage of "investment" instruments and transactions.²⁰ Consequently, it has

¹⁶ In many instances, the literal interpretation of a statute will be extended or restricted "to include situations which would reasonably have been contemplated by the legislature in light of the background and purposes giving impetus to the legislation." 2A SUTHERLAND, *supra* note 5, at § 54.05. Thus, although the statutory language may appear unambiguous, if a literal interpretation of the law leads to an absurd result or is inconsistent with legislative purpose, the express words must be modified so as to be harmonious with legislative intent. *Id.*, at §§ 46.01-.07; 3 *id.* at §§ 60.01, 60.03.

¹⁷ See H.R. REP. No. 1383, 73d Cong., 2d Sess. 30 (1934); S. REP. No. 792, 73d Cong., 2d Sess. 3-5 (1934); H.R. REP. No. 85, 73d Cong., 1st Sess. 2-3 (1933); S. REP. No. 47, 73d Cong., 1st Sess. 1 (1933). According to Sutherland, an accurate assessment of legislative history should include "information concerning the activities of pressure groups, economic conditions in the country during times when the legislation in question was under consideration, prevailing business practices, and the prior state of the law" 2A SUTHERLAND, *supra* note 5, at § 48.04. It has been said that the securities legislation and regulations were precipitated to a large degree by "underlying social and economic elements, such as the rise of the great national corporation, the separation of ownership from control, the diffusion of share ownership among an increasing segment of the population, and . . . [the] vast share of the national wealth represented by corporate securities" Loomis, *The Securities Exchange Act of 1934 and the Investment Advisers Act of 1940*, 28 GEO. WASH. L. REV. 214, 214-15 (1959).

¹⁸ *United Housing Foundation, Inc. v. Forman*, 421 U.S. 837, 849 (1975).

¹⁹ *Id.* Relying upon the language of an earlier decision, the Court in *Tcherepnin v. Knight*, 389 U.S. 332 (1967), stated that the term "security" "embodies a flexible rather than a static principle, one that is capable of adaptation to meet the countless and variable schemes devised by those who seek the use of the money of others on the promise of profits." 389 U.S. at 338 (citing *SEC v. W.J. Howey Co.*, 328 U.S. 293, 299 (1946)). This view of the 1934 Act has been reiterated in numerous subsequent decisions. See, e.g., *Superintendent v. Bankers Life & Cas. Co.*, 404 U.S. 6 (1971), wherein the Court stated that § 10(b) of the 1934 Act is read "to mean that Congress meant to bar deceptive devices and contrivances in the purchase or sale of securities whether conducted in the organized markets or face to face." *Id.* at 12.

²⁰ See note 17 and accompanying text *supra*.

been convincingly maintained by numerous authorities that the statutory language defining security should not be literally construed,²¹ as Congress was not concerned with exercising regulatory control over either personal or strictly commercial promissory notes,²² but rather with protecting the public in investment-oriented transactions.

Absent congressional mandate to the contrary, it now appears that the literal approach to construction of the definitional sections of the 1933 and 1934 Acts has been dealt its death blow by the Supreme Court, which rejected the theory outright in *United Housing Foundation, Inc. v. Forman*.²³ In *Forman*, which involved a determination as to the status under the securities laws of shares in a public cooperative apartment, the Court of Appeals for the Second Circuit apparently had injected new life into the literalist view. The Second Circuit panel had held that such shares were securities within the meaning of the federal securities laws, reasoning that "if a given instrument is a share of stock 'on its face' it is literally within the ambit of the statute."²⁴ Although the Second Circuit recognized the principle of "substance over form," it posited that this maxim should be utilized only to extend and not to restrict the coverage of

²¹ See, e.g., *C.N.S. Enterprises, Inc. v. G. & G. Enterprises, Inc.*, 508 F.2d 1354 (7th Cir.), cert. denied, 423 U.S. 825 (1975); *McClure v. First Nat'l Bank*, 497 F.2d 490 (5th Cir. 1974), cert. denied, 420 U.S. 930 (1975); *Bellah v. First Nat'l Bank*, 495 F.2d 1109 (5th Cir. 1974); *Lino v. City Investing Co.*, 487 F.2d 689 (3d Cir. 1973); *United States v. Koenig*, 388 F. Supp. 670 (S.D.N.Y. 1974); *Oxford Fin. Cos. v. Harvey*, 385 F. Supp. 431 (E.D. Pa. 1974). See also *United Housing Foundation, Inc. v. Forman*, 421 U.S. 837 (1975); *Tcherepnin v. Knight*, 389 U.S. 332 (1967); *SEC v. W.J. Howey Co.*, 328 U.S. 293 (1946); *SEC v. C.M. Joiner Leasing Corp.*, 320 U.S. 344 (1943), discussed in 17 S. CAL. L. REV. 324 (1944). Notwithstanding the fact that the *Joiner* Court stated that "[i]nstruments may be included within any of [the Acts'] definitions, as a matter of law, if on their face they answer to the name or description," 320 U.S. at 351, the *Forman* Court found that *Joiner* did not adopt the literal approach to the definitional sections of the statutes. The *Forman* Court explained that by using the conditional words "may" and "might" in . . . dicta the [*Joiner*] Court made clear that it was not establishing an inflexible rule barring inquiry into the economic realities underlying a transaction . . . , [but rather] intended only to make the rather obvious point that . . . most instruments bearing these traditional titles are likely to be covered by the statutes.

421 U.S. at 850 (footnote omitted).

²² See H.R. REP. No. 152, 73d Cong., 1st Sess. 24 (1933), discussed in Comment, *Commercial Notes and Definitions of 'Security' Under Securities Exchange Act of 1934: A Note is a Note is a Note?*, 52 NEB. L. REV. 478, 487 n.36 (1973) [hereinafter cited as *Commercial Notes*].

²³ 421 U.S. 837 (1975), rev'g *Forman v. Community Servs., Inc.*, 500 F.2d 1246 (2d Cir. 1974).

²⁴ 500 F.2d at 1252. The court stated that "[i]t would be anomalous . . . were one who was defrauded as to the nature of the instrument, 'stock' on its face, to be deprived of antifraud provisions directed at 'stock' transactions." *Id.*

the Acts.²⁵ Emphasizing, once again, that the courts must look to the economic realities of the transaction, the Supreme Court reversed the Second Circuit's ruling that the cooperative shares were securities, thereby rejecting a strictly literal construction of the statutory definition.²⁶ It is submitted that in the wake of the *Forman* decision, the question is not whether a promissory note is a security, but rather in which instances will a promissory note be deemed a security.

ALTERNATIVES TO THE LITERAL APPROACH

Those courts which have rejected the literal approach for the most part have relied upon the "unless the context otherwise requires" language as indicative of congressional intent to include within the purview of the securities laws only investment-oriented transactions and not every transaction involving a note.²⁷ As a consequence, judicial initiative has been directed towards the fashioning of a test which would identify readily those contexts which are sufficiently investment-oriented to render the promissory note a security.²⁸ The Supreme Court was presented with its first oppor-

²⁵ *Id.* at 1253.

²⁶ 421 U.S. at 837. The District Court for the Southern District of New York initially had held that cooperative housing shares did not become securities merely because the shares were designated as stock. See 366 F. Supp. 1117, 1126-27 (S.D.N.Y. 1973). Furthermore, according to the district court, "the fundamental nonprofit nature of th[e] transaction [presented an] . . . insurmountable barrier to" the argument that the transaction involved securities. *Id.* at 1128 (footnote omitted). The Second Circuit reversed on the ground that labeling the shares as stock rendered them securities within the meaning of the 1933 and 1934 Acts. The Second Circuit did go on to note, however, that even if a profit-seeking venture were required in order for federal securities laws to apply, profits in this transaction were present in the form of reduced rents, tax benefits, and income produced from the commercial facilities of the development. 500 F.2d at 1254-55. Relying on *Church of the Holy Trinity v. United States*, 143 U.S. 457 (1892) in which it was stated "a thing may be within the letter of the statute and yet not within the statute, because not within its spirit, nor within the intention of its makers," *id.* at 459, the Supreme Court reversed the Second Circuit and thereby refused to be confined by the literal language of the statutes. 421 U.S. at 849. While observing that the name attached to an instrument is not wholly irrelevant, the Court stressed that the application of the securities laws should turn on the economic realities underlying a transaction and that the protection of federal law should not be extended to purchasers of "stock" who intended only to acquire a residential apartment in a state-subsidized cooperative and had not invested for profit. *Id.* at 851.

²⁷ But see Hammett, *supra* note 12, at 38-40; *Notes as Securities*, *supra* note 11, at 239, wherein the author argues that the "proper construction appears to be that 'context' refers to the context of the statute."

²⁸ It should be noted that the tests which have been devised for determining whether a particular transaction is governed by the securities laws have not all arisen in the context of promissory note transactions. The definitional dilemma also is present in situations involving the meaning of "stock" and "investment contract," as well as any note. See, e.g., *United*

tunity to construe the definitional section of the 1934 Act in *Tcherepnin v. Knight*,²⁹ which involved the issue whether withdrawable capital shares constitute securities within the meaning of the 1934 Act.³⁰ Pointing to the long-standing canon of statutory construction that remedial legislation should be construed liberally to effectuate its purposes, the *Tcherepnin* Court held that "in searching for the meaning and scope of the word security in the Act, form should be disregarded for substance and the emphasis should be on economic reality."³¹ Finding that the issuance of withdrawable capital shares was a means of raising funds and that the shares in question most closely resembled investment contracts, the Court held them to constitute securities within the meaning of the 1934 Act.³²

This "substance over form" or "economic realities" method of analysis had been central to the Supreme Court's oft-cited decision in *SEC v. W.J. Howey Co.*³³ In that case, the Court found that "an offering of units of a citrus grove development coupled with a contract for cultivating, marketing, and remitting the net proceeds to the investor"³⁴ was an investment contract within the scope of the 1933 Act. Rejecting the view that a name or description appearing on the face of an instrument should be dispositive of the issue, the *Howey* Court articulated the substance over form approach later employed in *Tcherepnin*.³⁵ The Court stated that in order to determine whether an exchange is of the kind Congress intended to regulate, the events surrounding the transaction should be examined carefully.³⁶ To guide courts and practitioners in making this determination, the *Howey* Court laid down a three-pronged test: under the Securities Act of 1933, an investment contract is "a contract, transaction or scheme whereby a person invests his money in a

Hous. Found., Inc. v. Forman, 421 U.S. 837 (1975) (stock); *SEC v. W.J. Howey Co.*, 328 U.S. 293 (1946) (investment contract); *Exchange Nat'l Bank v. Touche Ross & Co.*, 544 F.2d 1126 (2d Cir. 1976) (promissory note). Interestingly, the Supreme Court has not addressed the precise issue whether all transactions involving promissory notes are governed by the federal securities laws and hence has not yet expressly rejected the literal approach in a promissory note situation.

²⁹ 389 U.S. 332 (1967).

³⁰ *Id.* at 333-34.

³¹ *Id.* at 336.

³² *Id.* at 338.

³³ 328 U.S. 293 (1946).

³⁴ *Id.* at 294. The Court pointed out that "[e]ach prospective customer is offered both a land sales contract and a service contract While the purchaser is free to make arrangements with other service companies, . . . 85% of the acreage sold . . . was covered by service contracts with defendant." *Id.* at 295.

³⁵ *Id.* at 300.

³⁶ *Id.* at 298-99.

common enterprise and is led to expect profits solely from the efforts of the promoter or a third party"³⁷ This standard has survived to the present time with but one slight modification; instead of requiring that the profits result solely from the efforts of others, the test apparently now is satisfied if the profits result substantially from the efforts of others.³⁸ The *Howey* test has come to be viewed as "embod[ying] the essential attributes that run through all of the Court's decisions defining security. The touchstone is the presence of an investment in a common venture premised on a reasonable expectation of profits to be derived from the entrepreneurial or managerial efforts of others."³⁹

A different version of the economic realities approach was employed in *McClure v. First National Bank*⁴⁰ and *Lino v. City Investing Co.*⁴¹ In *McClure*, the Fifth Circuit was confronted with the question whether the exchange of a promissory note and trust deed for a bank loan amounts to the transfer of a security.⁴² The Third Circuit in *Lino* addressed the issue whether the purchase of two franchise sales center licensing agreements for which payment was made partially in cash and partially with promissory notes involved the purchase of a security.⁴³ Relying upon the "unless the context otherwise requires" language of the 1933 and 1934 Acts' definitional sections, both the *McClure* and *Lino* courts held that Congress intended only "investment," and not "commercial" notes to be within the ambit of those Acts.⁴⁴ Unfortunately, in enunciating this varia-

³⁷ *Id.*

³⁸ See *Lino v. City Investing Co.*, 487 F.2d 689, 692 (3d Cir. 1973); *SEC v. Glenn W. Turner Enterprises, Inc.*, 474 F.2d 476, 482-83 (9th Cir.), *cert. denied*, 414 U.S. 821 (1973); note 110 *infra*.

³⁹ *United Hous. Found., Inc. v. Forman*, 421 U.S. 837, 852 (1975). But see Hannan & Thomas, *The Importance of Economic Reality and Risk in Defining Federal Securities*, 25 *HASTINGS L.J.* 219 (1974), where the authors contend that "[t]he definition of the term 'security' as used in the principal federal securities laws, is for the most part one of the best kept secrets in recent legal history."

⁴⁰ 497 F.2d 490 (5th Cir. 1974), *cert. denied*, 420 U.S. 930 (1975).

⁴¹ 487 F.2d 689 (3d Cir. 1973).

⁴² 497 F.2d at 491.

⁴³ 487 F.2d at 690.

⁴⁴ 497 F.2d at 492; 487 F.2d at 694-95. The *Lino* court concluded that the context of the transaction required a finding that a purchase of a security was not involved. The court stated that "[t]hese were personal promissory notes issued by a private party. There was no public offering of the notes, and the issuer was the person claiming to be defrauded. The notes were not procured for speculation or investment" 487 F.2d at 694-95. The investment-commercial dichotomy recognized in these cases has received extensive analysis by the commentators. See, e.g., Lipton & Katz, "Notes" are not Always Securities, 30 *BUS. LAW.* 763 (1975); Lipton & Katz, "Notes" are (are not?) Always Securities—A Review, 29 *BUS. LAW.* 861 (1974); Pollock, *supra* note 4.

tion of the economic realities test, the courts failed to propose detailed working definitions of the terms "commercial" and "investment," prompting critics of these decisions to argue that the commercial-investment dichotomy merely serves to confuse rather than clarify the issue.⁴⁵ It must be noted, however, that while neither *McClure* nor *Lino* enunciated clear and decisive formulae, both courts did suggest certain factors which serve to distinguish investment from commercial transactions. For instance, the *McClure* panel, in deciding that the notes in question were commercial in nature, emphasized that these instruments were "neither offered to [a] . . . class of investors, nor were they acquired . . . for speculation or investment."⁴⁶ Similarly, the *Lino* court justified its refusal to find a purchase of securities by pointing to the lack of a public offering and the absence of any indication that the instruments were "procured for speculation or investment."⁴⁷

Still another facet of the substance over form test surfaced in *Silver Hills Country Club v. Sobieski*,⁴⁸ wherein the California Supreme Court considered the definition of a security within the meaning of that state's securities law. The *Silver Hills* case involved the sale of charter memberships to finance the organization and construction of a private country club. Individuals purchasing these memberships were entitled to the use of the club's facilities, but were not entitled to share in the profits or income of the club.⁴⁹ Deeming this transaction to be one not involving a security, the *Silver Hills* court emphasized that two elements were necessary for

⁴⁵ See Hammett, *supra* note 12, at 41, 59-61, wherein the author argued that the latent ambiguity of the investment-commercial test is clearly visible in situations involving bank loans. The Fifth Circuit has taken the position that no transaction involving a bank loan involves the transfer of a security within the scope of the 1933 and 1934 Acts. See, e.g., *McClure v. First Nat'l Bank*, 497 F.2d 490, 495 (5th Cir. 1974), wherein the court stated that "[a] commercial bank's business is lending money not trading in securities." In *Great W. Bank & Trust v. Kotz*, 532 F.2d 1252, 1257 (9th Cir. 1976) (per curiam), the Ninth Circuit, citing *McClure*, disagreed stating that "[i]t is not enough to conclude *ipse dixit*: 'A commercial bank's business is lending money not trading in securities' . . . [since] banks may and do trade in securities." (citation omitted). The Ninth Circuit conceded, however, that promissory notes "given to a bank in the course of a commercial financing transaction" are not securities within the meaning of the federal securities laws: "To expand the reach of those acts to ordinary commercial loan transactions would distort congressional purpose as we interpret it." *Id.* at 1260. It would appear equally contrary to congressional intent, however, to exclude from the coverage of the securities acts all notes received by banks without a careful examination of the nature of each individual transaction. See notes 112-13 and accompanying text *infra*.

⁴⁶ 497 F.2d at 493.

⁴⁷ 487 F.2d at 694-95.

⁴⁸ 55 Cal. 2d 811, 361 P.2d 906, 13 Cal. Rptr. 186 (1961).

⁴⁹ *Id.* at 812, 361 P.2d at 907, 13 Cal. Rptr. at 187.

a security to exist: First, an investor must furnish initial value, and second, he must simultaneously assume the risk of possible loss of that value through operation of the promoter's enterprise.⁵⁰ Appropriately designated the "risk-capital" approach, the *Silver Hills* test is based on the court's belief that risk to one's initial investment is the most significant characteristic of a security.⁵¹ The risk-capital analysis recently was applied in the federal arena by the Ninth Circuit in *Great Western Bank & Trust v. Kotz*.⁵² In holding that a renewable note received in connection with a loan agreement did not constitute a security, the *Great Western* court suggested that the factors involved in determining whether a lender has invested risk capital in return for a security include time of maturity of the note, the existence and extent of collateralization, the circumstances of issuance, the relationship between the amount borrowed and the size of the borrower's business, as well as the contemplated use of the proceeds.⁵³

The Supreme Court's most recent opportunity to address the

⁵⁰ *Id.* at 814, 361 P.2d at 908, 13 Cal. Rptr. at 188. The *Silver Hills* rationale is discussed and analyzed in Note, *The Definition of a Security Under the California Corporate Securities Law of 1968: The Risk Capital Test*, 6 PAC. L.J. 683, 689-99 (1975).

⁵¹ The core of the *Silver Hills* rationale later was incorporated into the often-cited definition of a security formulated by Professor Coffey. See Coffey, *The Economic Realities of a "Security": Is There a More Meaningful Formula?*, 18 W. RES. L. REV. 367, 377 (1967). Professor Coffey's formula states:

A "security" is:

(1) A transaction in which

(2) a person ("buyer") furnishes value ("initial value") to another ("seller"); and

(3) a portion of initial value is subjected to the risks of an enterprise, it being sufficient if—

(a) part of initial value is furnished for a proprietary interest in, or debt-holder claim against, the enterprise, or

(b) any property received by the buyer is committed to use by the enterprise, even though the buyer retains specific ownership of such property, or

(c) part of initial value is furnished for property whose present value is determined by taking into account the anticipated but unrealized success of the enterprise, even though the buyer has no legal relationship with the enterprise; and

(4) at the time of the transaction, the buyer is not familiar with the operations of the enterprise or does not receive the right to participate in the management of the enterprise; and

(5) the furnishing of initial value is induced by the seller's promises or representations which give rise to a reasonable understanding that a valuable benefit of some kind, over and above initial value, will accrue to the buyer as a result of the operation of the enterprise.

Id. (footnote omitted).

⁵² 532 F.2d 1252 (9th Cir. 1976) (per curiam).

⁵³ *Id.* at 1257-58.

definitional issue arose in *United Housing Foundation, Inc. v. Forman*,⁵⁴ in which it was held that shares in a nonprofit cooperative housing project are not securities. By relying chiefly upon the absence of any expectation of profits on the part of the purchasers—who, according to the Court, were interested primarily in acquiring adequate low-cost housing⁵⁵—the *Forman* decision injected new vitality into the *Howey* formula⁵⁶ and solidified its role as controlling authority in identifying an investment contract. Of necessity, this reaffirmation of the *Howey* standard has influenced subsequent decisions of other courts faced with the definitional question, whether involving the proper interpretation of “stock,” “note,” or “investment contract.”⁵⁷ Soon after the *Forman* decision the Second Circuit, in *Exchange National Bank v. Touche Ross & Co.*,⁵⁸ was presented with an opportunity to consider the definitional issue. In that case, three promissory notes had been transferred by a stock brokerage firm to secure a loan from the plaintiff bank.⁵⁹ The court rejected the defendant’s contention that the notes evidenced an ordinary commercial loan not subject to the 1933 and 1934 Acts.

⁵⁴ 421 U.S. 837 (1975). Numerous commentators have discussed *Forman* and its impact on the definitional issue. See, e.g., 1975 B.Y.U.L. REV. 849; 9 LOY. L.A.L. REV. 206 (1975); 54 N.C.L. REV. 731 (1976).

⁵⁵ 421 U.S. at 851. Defining profit as “capital appreciation” or a “participation in earnings resulting from the use of investors’ funds,” the Court refused to recognize as profits reduced rental charges or tax benefits realized as a result of ownership of co-op shares. *Id.* at 852-55. Acknowledging that income from commercial leases is a type “of profit traditionally associated with a security investment,” the Court went on to hold that income received by the co-op corporation from the leasing of various commercial facilities was too insubstantial and speculative “to bring the entire transaction within the Securities Acts.” *Id.* at 855-56.

⁵⁶ See 54 N.C.L. REV. 731 (1976), wherein it is pointed out that “[t]he Court’s principal tool for distinguishing a security from other interests is the test developed in *SEC v. W.J. Howey Co.* *Forman* refined the test so that now a transaction comes within the definitional sections . . . whenever investors are motivated to risk their capital by a *significant, realistic* expectation of *substantial* profits . . . to come solely from the efforts of others.” *Id.* at 732-33 (footnotes omitted) (emphasis in original).

⁵⁷ See, e.g., *Exchange Nat’l Bank v. Touche Ross & Co.*, 544 F.2d 1126 (2d Cir. 1976) (promissory notes held to be securities); *Grenader v. Spitz*, 537 F.2d 612 (2d Cir.), *cert. denied*, 429 U.S. 1009 (1976) (shares in private cooperative apartment held not to be securities). Although the *Exchange* court failed to see the relevance of the *Howey* formula in the context of promissory notes since the test was fashioned specifically to cover situations involving investment contracts, the Second Circuit nevertheless adhered to the anti-literalist approach of *Forman* by holding that the express language of the statute controls unless it is established by one of the parties that “the context otherwise requires.” 544 F.2d at 1137. See notes 58-65 and accompanying text *infra*.

⁵⁸ 544 F.2d 1126 (2d Cir. 1976).

⁵⁹ *Id.* at 1128. The complaint alleged that the brokerage firm’s financial statements, certified by the defendant, were materially false and misleading and that the defendant knew or should have known this fact. The firm eventually was forced into receivership, and the notes became worthless. *Id.*

Framing its examination of the issue around the "unless the context otherwise requires" language, the Second Circuit ruled that the party attempting to show that a note is not a security has the burden of proving that the context in which the note was issued removes it from the operation of the securities law.⁶⁰ In reaching its conclusion that defendant Touche Ross failed to satisfy this burden, the panel declined to adhere to any previously delineated test for evaluating the status of a particular instrument as a security; instead, the court formulated its own test based primarily not on a view toward what a security is but on what it is not. Stating that certain types of notes clearly were not intended by Congress to fall within the coverage of the 1934 Act,⁶¹ the Second Circuit concluded that any note "bearing a strong family resemblance" to these excluded notes should likewise be deemed without the scope of the statute.⁶² Since the notes in question were more closely akin to investment instruments than unregulated commercial instruments, the provisions of the 1934 Act were held to be applicable.⁶³ While the *Exchange* panel purported to reject the *Howey* test as irrelevant in promissory note situations,⁶⁴ it is submitted that the *Exchange* test is, in essence, a context-over-text approach: Congressional intent was the focal point of analysis, and an investment-commercial dichotomy was pivotal to the Court's ultimate determination.⁶⁵

⁶⁰ *Id.* at 1137-38. The Second Circuit's decision in *Exchange* seems contrary to previously well-recognized precepts concerning the burden of proof in securities cases. By holding that the burden of proof is on the party asserting that an item is not a security, the court contradicted the principle that the person invoking federal jurisdiction, *i.e.*, the plaintiff, must establish it by proving the purchase or sale of a security. See Note, *Bank Loans as Securities*, 51 ST. JOHN'S L. REV. 440, 443 n.15 (1977).

⁶¹ The court listed consumer financing notes, home mortgage notes, secured short-term loans to small businesses, "character" loans to bank customers, short-term notes secured by accounts receivable, and notes which merely formalize open-account debts "incurred in the ordinary course of business," as representative of those notes which do not fall within coverage of the securities acts. 544 F.2d at 1138.

⁶² *Id.*

⁶³ *Id.* at 1138-39. Many factors influenced the Second Circuit's ultimate holding that the notes in question were securities. The subordination of the notes to claims of other general creditors, the use of the proceeds as "equity capital," and the absence of collateral were viewed by the court as particularly indicative of an investment transaction. This conclusion has been criticized by one student author who viewed the notes in *Exchange* as commercial rather than investment in light of tests utilized by other courts. See Note, *Bank Loans as Securities*, 51 ST. JOHN'S L. REV. 440, 449-52 (1977).

⁶⁴ 544 F.2d at 1136-37.

⁶⁵ The *Exchange* "family resemblance" test is examined in Pollock, *supra* note 4, at 545-47, wherein the author labeled it the "purpose" test. According to this commentator, "[a]lthough the court never discussed the meaning directly, its language throughout the opinion made clear that it was reading 'unless the context otherwise requires' to mean 'unless the context otherwise requires to carry out the purposes of the securities acts.'" *Id.* at 546

THE NEED FOR UNIFORMITY AND FLEXIBILITY

The decision whether to characterize a particular note as a security is extremely significant, as ultimate rights and remedies are influenced by it. Most importantly, labeling a promissory note as a security affords a defrauded claimant access to the federal courts. A plaintiff who is able to pursue his cause of action in a federal forum under the antifraud provisions of the 1934 Act receives significant substantive and procedural benefits.⁶⁶ Procedurally, a number of factors accentuate the attractiveness of the federal court system, ranging from the initial advantages of liberal in personam jurisdiction and venue requirements in the 1934 Act⁶⁷ to the fact that a judgment rendered in the action is enforceable nationwide.⁶⁸ Of crucial importance as well are the substantive advantages of a federal cause of action. Application of the Securities Exchange Act in many cases facilitates a defrauded plaintiff's recovery. A plaintiff commencing a rule 10b-5 suit, for example, may select his adversary from a potentially larger class of individuals since the plaintiff need

(footnote omitted) (emphasis in original). Under this analysis, every note would be covered by the securities laws unless it could be shown that no congressional purpose would be furthered by the application of those statutes. Although this commentator expressed his preference for the purpose test when applied in light of congressional intent, he went on to note that even this test may result in subjective, arbitrary decisions if courts do not frame a properly narrow statement of congressional purpose. *Id.* at 547. For a brief analysis of *Exchange*, see 30 VAND. L. REV. 110 (1977), wherein it is suggested that a listing of commercial note transactions should be compiled and that "all notes [should be] presumed to be securities unless [they fit] within one of the enumerated examples of commercial note transactions." *Id.* at 120-21.

⁶⁶ See Hammett, *supra* note 12, at 30-35. While application of the 1933 and 1934 Acts may benefit an aggrieved claimant, it imposes substantial duties upon the maker of an instrument. Pursuant to § 5 of the 1933 Act, the issuer of a promissory note which is considered a security would have to comply with the Act's often expensive and time-consuming registration requirements. See Securities Act of 1933, § 5, 15 U.S.C. § 77e (1970); 54 N.C.L. REV. 731 (1976). Section 3 of the 1933 Act, however, exempts certain promissory notes from the registration requirements. See Securities Act of 1933, § 3, 15 U.S.C. § 77c(a)(3) (1970). Failure to comply with the registration requirements where a nonexempt security is involved may lead to the imposition of harsh sanctions. See Securities Act of 1933, §§ 12, 15, 15 U.S.C. §§ 77l, 77o.

⁶⁷ Securities Exchange Act of 1934, § 27, 15 U.S.C. § 78aa (1970) provides in part: Any criminal proceeding may be brought in the district wherein any act or transaction constituting the violation occurred. Any suit or action to enforce any liability or duty created by this chapter . . . , or to enjoin any violation . . . , may be brought in any such district or in the district wherein the defendant is found or is an inhabitant or transacts business, and process in such cases may be served in any other district of which the defendant is an inhabitant or wherever the defendant may be found.

See *Sargent v. Genesco, Inc.*, 492 F.2d 750, 759 (5th Cir. 1974).

⁶⁸ See Hammett, *supra* note 12, at 30-31, 31 nn.29-30.

not be in privity with the party guilty of the misrepresentation.⁶⁹ In addition, it is not necessary that there be an agency relationship between the potential defendant and the person who made the misrepresentation; rather, liability may be imposed upon those who are in "control" of the violators of the Act.⁷⁰ Moreover, the permissibility of imposing 10b-5 liability for encouraging or aiding the defrauding of an investor is in marked contrast to common law principles.⁷¹

Another advantage of the 10b-5 fraud action permits the maker of a note, as seller, to seek redress against payees, whereas state blue-sky laws traditionally permit only purchasers to recover.⁷² Greater ease of recovery under the 1934 Act also is assured by a burden of proof less exacting than the one customarily imposed upon a plaintiff in a common law fraud action;⁷³ while at common

⁶⁹ Promulgated by the Securities and Exchange Commission pursuant to section 10(b) of the 1934 Act, 15 U.S.C. § 78j(b) (1970), rule 10b-5, 17 C.F.R. § 240.10b-5 (1977), states:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

(a) To employ any device, scheme, or artifice to defraud,

(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

⁷⁰ Under common law principles, an agency relationship is a condition precedent to the imposition of liability upon individuals who have not personally consummated a fraudulent transaction. Pursuant to provisions of the 1934 Act, however, an aggrieved claimant may maintain an action against a much larger group of defendants. See *Gottlieb v. Sandia Am. Corp.*, 452 F.2d 510, 516 (3d Cir.), *cert. denied*, 404 U.S. 938 (1971). This expansion of liability is a result of § 20(a) of the 1934 Act which provides:

Every person who, directly or indirectly, controls any person liable under any provision of this chapter or of any rule or regulation thereunder shall also be liable jointly and severally with and to the same extent as such controlled person to any person to whom such controlled person is liable, unless the controlling person acted in good faith and did not directly or indirectly induce the act or acts constituting the violation or cause of action.

15 U.S.C. § 78t(a) (1970). By liberally construing the words "controlling person," the courts have enhanced the distinction between the 1934 Act and the common law rule. Although the term has not yet been defined with precision, it is clear that something less than a strict agency relationship will suffice as a prerequisite to liability under § 20(a). See, e.g., *Ayers v. Wolfenbarger*, 491 F.2d 8 (5th Cir. 1974).

⁷¹ See, e.g., *Sargent v. Genesco, Inc.*, 492 F.2d 750, 759-61 (5th Cir. 1974); *Ayers v. Wolfenbarger*, 491 F.2d 8, 13-15 (5th Cir. 1974). See generally Comment, *The Status of the Promissory Note Under the Federal Securities Laws*, 1975 ARIZ. ST. L.J. 175, 177 n.14.

⁷² See *Commercial Notes*, *supra* note 22.

⁷³ See *Stevens v. Vowell*, 343 F.2d 374, 379 (10th Cir. 1965); *Royal Air Properties, Inc. v. Smith*, 312 F.2d 210, 212 (9th Cir. 1962); *Hooper v. Mountain States Sec. Corp.*, 282 F.2d 195, 201 (5th Cir. 1960); *Whitlow & Assocs. v. Intermountain Brokers, Inc.*, 252 F. Supp. 943,

law a claimant must establish specific reliance upon the defendant's misstatements or omissions as a prerequisite to recovery, under rule 10b-5 a plaintiff need only show that the misrepresentations were material.⁷⁴ Lastly, a 10b-5 claimant is afforded the advantages inherent in the 1934 Act's anti-waiver provisions⁷⁵ together with the benefits of the Federal Rules of Civil Procedure⁷⁶ and liberal discovery techniques.⁷⁷ With these major substantive and procedural advantages at stake, there is little doubt that an individual claiming to have been defrauded in a transaction involving the exchange of a promissory note would much prefer the opportunity to seek relief in a federal forum, the availability of which is dependent upon the classification of a promissory note as a security.⁷⁸

947 (D. Haw. 1966); *SEC v. Gulf Intercontinental Fin. Corp.*, 223 F. Supp. 987, 993 (S.D. Fla. 1963).

⁷⁴ See *Affiliated Ute Citizens v. United States*, 406 U.S. 128 (1972) wherein the Court stated:

[P]ositive proof of reliance is not a prerequisite to recovery. All that is necessary is that the facts withheld be material in the sense that a reasonable investor might have considered them important in the making of this decision. This obligation to disclose and this withholding of a material fact establish the requisite element of causation in fact.

Id. at 153-54 (citation omitted). See *Simon v. Merrill, Lynch, Pierce, Fenner & Smith, Inc.*, 482 F.2d 880, 884 (5th Cir. 1973); *List v. Fashion Park, Inc.*, 340 F.2d 457, 463 (2d Cir.), *cert. denied*, 382 U.S. 811 (1965); Hammett, *supra* note 12, at 32; *Notes as Securities*, *supra* note 11, at 233 n.4; *Commercial Notes*, *supra* note 22, at 505.

Although some authorities indicated that a plaintiff could predicate a private damage action upon negligent misstatements under § 10(b) and rule 10b-5, the Supreme Court decision in *Ernst & Ernst v. Hochfelder*, 425 U.S. 185 (1976), definitively held that scienter is a requisite element in such a suit. The Court in *Hochfelder* reasoned that the language of section 10(b) proscribes intentional or willful conduct designed to deceive investors and that therefore liability may not be imposed upon a defendant absent a showing of scienter. See generally Van Graafeiland, *Foreword: A Lawyer's Observations on Hochfelder*, 51 ST. JOHN'S L. REV. 239 (1977).

⁷⁵ Section 29(a) of the 1934 Act invalidates "[a]ny condition, stipulation, or provision binding any person to waive compliance with any provision of this chapter or of any rule or regulation thereunder, or of any rule of an exchange required thereby" 15 U.S.C. § 78cc(a) (1970). In *Wilko v. Swan*, 346 U.S. 427 (1953), a similar provision of the Securities Act of 1933, § 14, 15 U.S.C. § 77n (1970), was held to negate a binding arbitration clause contained within a broker-customer agreement.

⁷⁶ The pleading, joinder, and class action provisions of the Federal Rules of Civil Procedure are generally more liberal and less formal than those which prevail in many state forums. See FED. R. CIV. P. 3-16, 18-21, 23.

⁷⁷ See FED. R. CIV. P. 26-37.

⁷⁸ It is important to note that the antifraud provisions of the 1933 and 1934 Acts are constitutionally predicated upon the direct or indirect use of an "instrumentality of interstate commerce or of the mails" Securities Exchange Act of 1934, § 10, 15 U.S.C. § 78j (1970). See *Olympic Capital Corp. v. Newman*, 276 F. Supp. 646, 653 (C.D. Cal. 1967); *SEC v. Gulf Intercontinental Fin. Corp.*, 223 F. Supp. 987, 993 (S.D. Fla. 1963). Hence, the mere existence of a promissory note characterizable as a security alone does not create a basis for federal jurisdiction.

Since the decisions in *McClure* and *Lino*, the crucial task confronting the judiciary and practitioners had been to distinguish satisfactorily an investment note from a commercial note. The absence of congressional guidance in this area has placed a tremendous burden upon individuals who are possibly subject to the anti-fraud provisions of the 1933 and 1934 Acts by virtue of a given exchange or transaction. Because the Supreme Court has not yet rendered a decision directly addressing the promissory note issue, no clear basis for drawing this distinction has been available. Although analogies have been drawn between cases involving notes and those involving investment contracts or stock, the latter cases may be considered no more than persuasive authority.⁷⁹ The unfortunate result has been that the determination whether a given promissory note is a security has depended, to some extent, upon the relative importance attached by a particular court to the factors considered.⁸⁰

The tests propounded thus far have failed to provide a predictable and uniform solution to the uncertainty surrounding the status of promissory notes as securities.⁸¹ Sporadic employment of one or

⁷⁹ Many recent cases addressing the definitional issue have arisen in contexts other than that of a promissory note transaction. See, e.g., *McGovery Plaza Joint Venture v. First of Denver Mortgage Investors*, [1977-1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 96,191 (10th Cir. Oct. 4, 1977) (neither a construction loan commitment nor permanent loan commitment were securities under 1933 and 1934 Acts); *Hirk v. Agri-Research Council, Inc.*, [1977-1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 96,167 (7th Cir. Sept. 6, 1977) (discretionary trading account did not constitute investment contract since investor's funds were not pooled with those of other investors); *Robinson v. UMW Health & Retirement Funds*, 435 F. Supp. 245 (D.D.C. 1977) (interest in pension or health plan is not a security); *Sullivan v. Chase Investor Serv., Inc.*, 434 F. Supp. 171 (N.D. Cal. 1977) (purchase of investment advisory services is not an investment contract); *Plunkett v. Francisco*, 430 F. Supp. 235 (N.D. Ga. 1977) (cattle lease agreement and calf maintenance agreement constituted investment contract where investor paid in advance for lease of pregnant cow and maintenance expenses as incurred); *Daniel v. International Brotherhood of Teamsters*, 410 F. Supp. 541 (N.D. Ill. 1976) (involuntary noncontributory employee pension fund is a security), noted in 5 *FORDHAM URB. L.J.* 591 (1977); 22 *VILL. L. REV.* 195 (1976).

⁸⁰ See, e.g., *Exchange Nat'l Bank v. Touche Ross & Co.*, 544 F.2d 1126 (2d Cir. 1976) (applying family resemblance text); *Grenader v. Spitz*, 537 F.2d 612 (2d Cir.), cert. denied, 429 U.S. 1009 (1976) (economic realities emphasized); *Great W. Bank & Trust v. Kotz*, 532 F.2d 1252 (9th Cir. 1976) (risk capital employed as determinative factor).

⁸¹ The shortcomings of the economic realities, risk capital, and purpose tests are discussed in Pollock, *supra* note 4, at 541-47. In discussing the risk capital test, Pollock criticized the *Great Western* court for the unpredictability of its approach. In particular, he argued that "[o]ne of the principal weaknesses of the risk capital test . . . is that the court offers no workable guidelines to determine what level of risk will be sufficient to convert a non-security note into a security. Consequently, the test is impossible to apply in a predictable manner." *Id.* It should be noted, however, that the *Great Western* court did not hold any single factor to be dispositive of the issue. Rather, it sought to differentiate between two somewhat nebu-

more of these suggested criteria has served only to increase the existing confusion. Unfortunately, no court has attempted to analyze the definitional problem in light of all the pertinent elements.⁸² A method of analysis which incorporates all of the factors isolated by the courts would seem to provide a framework within which a more meaningful evaluation of the status of promissory notes may be conducted. While the indefiniteness which now characterizes the standards applied by the federal courts may not be entirely eradicated through such an approach, it is suggested that an overly concrete mode of analysis would deprive the courts of that flexibility which is indispensable in this area of the law. Due to the variety of contexts in which instruments might be involved, a formula which leaves some discretion in the hands of the judiciary appears necessary;⁸³ a precise, overly-rigid rule would seem less workable than those tests which presently exist.⁸⁴ It is submitted that a proper mode of analysis would be predicated upon the basic assumption that the economic realities of the transaction should govern the applicability of the federal securities laws. Each controversy therefore must be examined on an individual basis. While not definable in precise terms,⁸⁵ the factors that should be considered may be

lous concepts—risk capital and risky loan. 532 F.2d at 1257. The court recognized that “[i]n one sense every lender of money is an investor since he places his money at risk in anticipation of a profit in the form of interest. Also . . . every investor lends his money to a borrower who uses it for a price and is expected to return it one day.” *Id.*, (citing *C.N.S. Enterprises, Inc. v. G. & G. Enterprises, Inc.*, 508 F.2d 1354, 1359 (7th Cir.), *cert. denied*, 423 U.S. 825 (1975)). While there always may be some uncertainty as to whether a particular transaction warrants application of federal securities laws, the pertinent question is whether the risk inherent in the transaction goes beyond that normally associated with the lending of money for a period of time. The Ninth Circuit has attempted to set forth certain criteria to be considered in evaluating whether a given promissory note was “in economic reality a ‘security,’ received in exchange for the payee’s ‘investment.’” 532 F.2d at 1257.

⁸² The approach utilized by the Ninth Circuit in *Great W. Bank & Trust v. Kotz*, 532 F.2d 1252 (9th Cir. 1976), most closely epitomizes an all-inclusive standard. See notes 86-109 and accompanying text *infra*.

⁸³ The Supreme Court has stated that Congress sought to frame the definition of “the term ‘security’ in sufficiently broad and general terms so as to include within that definition the many types of instruments that in our commercial world fall within the ordinary concept of a security.” *United Hous. Found., Inc. v. Forman*, 421 U.S. 837, 847-48 (1975) (citing H.R. REP. NO. 85, 73d Cong., 1st Sess. 11 (1933)).

⁸⁴ Under an inflexible rule, for example, it is quite possible for a particular note to be characterized incorrectly. See note 112 *infra*. Compare *Exchange Nat’l Bank v. Touche Ross & Co.*, 544 F.2d 1126 (2d Cir. 1976) (notes evidencing bank loans afforded security status), with *McClure v. First Nat’l Bank*, 497 F.2d 490 (5th Cir. 1974), *cert. denied*, 420 U.S. 930 (1975) (notes given in connection with bank loans summarily denied security status).

⁸⁵ As one author has written: “It would be misleading to suggest that such an inquiry can ever be summarized in a neat formula or a short list of guidelines.” Comment, *The Status of the Promissory Note Under the Federal Securities Laws*, 1975 ARIZ. ST. L.J. 175, 192 (1975).

culled from the numerous cases addressing the definitional problem. Focusing on these criteria, courts can determine whether particular transactions deserve the protection of the securities laws. This type of analysis is typified by the Ninth Circuit opinion in *Great Western Bank & Trust v. Kotz*.⁸⁶

Beginning with the notion that the presence or absence of any single factor should not be dispositive of the promissory note issue, the *Great Western* court reasoned that "[w]hen all factors together are brought to bear" the transaction viewed in its entirety will reveal the note to be either investment or commercial in nature.⁸⁷ Although it highlighted the question whether the payee has contributed risk capital subject to the entrepreneurial or managerial efforts of others, the court also considered the time of maturity of the note, the extent of collateralization, the form of the obligation, the circumstances of issuance, the size of the borrower's business relative to the amount borrowed, and the contemplated use of the funds.⁸⁸ It is suggested, however, that the risk element should not be overemphasized to the exclusion of other factors, and that the inquiry thus should be directed towards the investment-commercial dichotomy with the risk element being only one of many factors examined.⁸⁹

Among the considerations that are relevant in determining whether a particular note should be deemed a security is the name which appears upon the face of the instrument. Hence, the characterization of an instrument on financial statements as a security may be indicative of an investment-oriented transaction.⁹⁰ Likewise relevant is the number and value amount of the notes which are issued.⁹¹ The exchange of a single note as part of an isolated transaction tends to suggest a personal or commercial climate, whereas investment notes frequently are issued in large numbers⁹² and gener-

⁸⁶ 532 F.2d 1252 (9th Cir. 1976).

⁸⁷ *Id.* at 1258.

⁸⁸ *Id.* at 1257-58.

⁸⁹ Several recent cases have employed the investment-commercial test and, relying heavily upon the absence of a profit motive, have concluded that particular promissory notes were intended to be cash substitutes and as such did not constitute securities. *See, e.g.,* EMISCO Indus., Inc. v. Pro's Inc., 543 F.2d 38, 40 (7th Cir. 1976); Altman v. Knight, 431 F. Supp. 309, 312 (S.D.N.Y. 1977); SEC v. Univest, Inc., 410 F. Supp. 1029, 1030-31 (N.D. Ill. 1976).

⁹⁰ *See, e.g.,* Sanders v. John Nuveen & Co., 463 F.2d 1075 (7th Cir.), *cert. denied*, 409 U.S. 1009 (1972). In support of its holding that certain promissory notes were securities within the meaning of the securities laws, the *Sanders* court observed that the notes were referred to as "short term open market paper" in the issuer's financial statements. 463 F.2d at 1079.

⁹¹ *See* *Great W. Bank & Trust v. Kotz*, 532 F.2d 1252, 1258 (9th Cir. 1976).

⁹² Several decisions holding promissory notes to be within the coverage of the antifraud provisions of the 1933 and 1934 Acts have involved public offerings. *See, e.g.,* Llanos v. United States, 206 F.2d 852 (9th Cir. 1953), *cert. denied*, 346 U.S. 923 (1954).

ally sold to a class consisting of many relatively sophisticated payees. The extent of collateralization also should be given weight in evaluating a promissory note transaction, since an unsecured lender certainly assumes a higher degree of risk. Furthermore, tremendous risk is present when the amount borrowed is a figure significantly in excess of the value of the borrower's business.⁹³ Should the payee of the note be afforded certain benefits normally arising only in the investment arena, such as the right to inspect the books and records of the issuer's enterprise, in return for which the payee assumes increased risk, the transaction is more likely to involve a security.⁹⁴ Such indicia are useful in distinguishing between what the *Great Western* court described as the risky loan and risk capital.⁹⁵

The manner in which promissory notes are to be repaid sheds additional light upon whether the particular note should be viewed as a security. Should the issuer's repayment be contingent upon the earning of potential profits or should the debt actually be payable solely out of projected earnings, an investment transaction would be evidenced.⁹⁶ One should also consider whether the payee is familiar with the nature and operations of the issuer's business; a lack of familiarity gives rise to a significantly increased risk factor.⁹⁷ The use to which a borrower puts the proceeds of a loan also should not be overlooked.⁹⁸ If the proceeds are merely expended on current business operations or used to acquire consumer products, the trans-

⁹³ See *Great W. Bank & Trust v. Kotz*, 532 F.2d 1252, 1228 (9th Cir. 1976) (citing *C.N.S. Enterprises, Inc. v. G. & G. Enterprises, Inc.*, 508 F.2d 1354, 1361 (7th Cir.), *cert. denied*, 423 U.S. 825 (1975)).

⁹⁴ See, e.g., *Tcherepnin v. Knight*, 389 U.S. 332, 337 (1967), wherein instruments found to be securities conferred voting rights upon the payees. See generally *Commercial Notes*, *supra* note 22, at 516-17.

⁹⁵ 532 F.2d at 1257-58. The risk capital approach recently was employed by the Ninth Circuit in *United Cal. Bank v. THC Financial Corp.*, [1977-1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 96,125 (9th Cir. July 25, 1977). The court found that a corporation's agreement to purchase on demand all notes taken by a bank as security for advances extended to another business did not constitute a security. In so ruling, the Ninth Circuit pointed out that no risk capital had been involved since the risk accompanying the notes was equivalent to the risk associated with the lending of any money for a period of time. Interestingly, the court explained that the risk capital test encompasses an economic realities standard as well as a *Howey*-type requirement that profits be expected to result from the entrepreneurial efforts of others. Summarizing its holding, the court stated that "participations or notes evidencing 'risk capital,' i.e., risk of non-payment, are securities while those evidencing 'risky loans' are not." *Id.* at 92,061.

⁹⁶ See *Commercial Notes*, *supra* note 22, at 517.

⁹⁷ See Coffey, *The Economic Realities of a "Security": Is There a More Meaningful Formula?*, 18 W. RES. L. REV. 367, 377 (1967), quoted in note 51 *supra*.

⁹⁸ See *Great W. Bank & Trust v. Kotz*, 532 F.2d 1252 (9th Cir. 1976). The *Great Western* court emphasized this factor as an element to be weighed in the risk capital balancing process.

action most likely is not within the purview of the securities law.⁹⁹ If the proceeds are utilized to finance the underlying capital foundation of an enterprise, however, the possibility that the note is a security is greatly enhanced. Related to this consideration is a notion frequently referred to as "transaction impetus." In general, advocates of this theory argue that a security transaction rarely exists when the purchaser initiated the dealings with the issuer.¹⁰⁰ In other words, a note is more likely to represent an investment when the origins of the transaction can be traced back to the efforts of the issuer.¹⁰¹ This argument has been criticized, however, since "a private party may also have surplus funds which need investment, and may initiate a financial transaction resulting in the acquisition of corporate securities."¹⁰² Nevertheless, it is suggested that the origin of the transfer should be considered along with the other available criteria.

Negotiability of an instrument may also give evidence of the nature of the note in some circumstances, although this element should not be overly emphasized since negotiable securities are now quite common in the financial arena.¹⁰³ The term of the note in question also should be examined, as short term obligations are very likely to be simple commercial instruments not subject to federal regulation.¹⁰⁴ Whether the issuer of a contested instrument deals

⁹⁹ See, e.g., *C.N.S. Enterprises, Inc. v. G. & G. Enterprises, Inc.*, 508 F.2d 1354, 1359-60 (7th Cir.), *cert. denied*, 423 U.S. 825 (1975) (notes given as payment for consumer goods are not securities); *McClure v. First Nat'l Bank*, 497 F.2d 490, 494-95 (5th Cir. 1974), *cert. denied*, 420 U.S. 930 (1975) (promissory notes utilized merely for commercial purposes are not securities).

¹⁰⁰ The transaction impetus notion was alluded to in decisions by both the Ninth and the Seventh Circuits. See *Great W. Bank & Trust v. Kotz*, 532 F.2d 1252, 1258 n.5 (9th Cir. 1976); *Sanders v. John Nuveen & Co.*, 463 F.2d 1075, 1080 (7th Cir.), *cert. denied*, 409 U.S. 1009 (1972).

¹⁰¹ See Comment, *The Status of Promissory Notes Under the Federal Securities Laws*, 1975 ARIZ. ST. L.J. 175.

¹⁰² *Great W. Bank & Trust v. Kotz*, 532 F.2d 1252, 1258 n.5 (9th Cir. 1976).

¹⁰³ See *id.*; *Commercial Notes*, *supra* note 22, at 522 n.165.

¹⁰⁴ It is quite likely that neither short-term promissory notes nor demand notes qualify as securities. See *Turner v. Commissioner*, 303 F.2d 94 (4th Cir. 1962). But see *Zeller v. Bogue Elec. Mfg. Corp.*, 476 F.2d 795 (2d Cir.), *cert. denied*, 414 U.S. 908 (1973). The *Zeller* court determined that where an issuer effectively can prevent demand by the purchaser, the demand note may be deemed a security. *Id.* at 799. In contrast, long-term notes often are found to be securities. Therefore, it is important to examine the time span between issuance and maturity when a note is payable on a specified future date. See, e.g., *Movielab, Inc. v. Berkey Photo, Inc.*, 452 F.2d 662 (2d Cir. 1971), the plaintiff had been fraudulently induced into exchanging its long-term promissory notes for the assets of another corporation. In holding that the entire transaction involved the exchange of a security, the court emphasized, *inter alia*, the 20-year term of the notes. *Id.* at 663.

personally with the payee on a face-to-face basis is another suggestive factor, since securities frequently are issued through neutral third parties with the national exchanges serving as the medium for the transfer.¹⁰⁵

Finally, it may prove valuable to examine the aforementioned factors against the backdrop of the criteria expressly enunciated by the *Howey* Court¹⁰⁶ and refined in the *Forman* decision.¹⁰⁷ To that end, an evaluation should be made concerning whether the transaction involved the transfer of money or other articles of value¹⁰⁸ toward a common enterprise¹⁰⁹ and whether the purchaser's primary motivation for entering into the exchange was the expectation of a benefit generated substantially through the efforts of the issuer or a third party,¹¹⁰ and not merely the desire to obtain a commodity.¹¹¹

An obvious corollary to the mode of analysis herein suggested is that the classification of entire transaction groups as either in-

¹⁰⁵ Compare *Lino v. City Investing Co.*, 487 F.2d 689 (3d Cir. 1973) (private transaction held not to be regulated by the 1933 and 1934 Acts), with *SEC v. Los Angeles Trust Deed & Mortgage Exch.*, 186 F. Supp. 830 (S.D. Cal.), modified on other grounds, 285 F.2d 162 (9th Cir. 1960), cert. denied, 366 U.S. 919 (1961) (public offering held to be governed by the securities acts).

¹⁰⁶ 328 U.S. at 298-99. It should be noted that one court has expressly rejected *Howey* as irrelevant to the promissory note situation, see note 57 *supra*, while another court has adopted the *Howey* formula in toto as the appropriate standard to be applied, see note 114 *infra*.

¹⁰⁷ 421 U.S. at 852.

¹⁰⁸ In addition to money, assets have been recognized as consideration for promissory notes. See, e.g., *SEC v. Continental Commodities Corp.*, 497 F.2d 516 (5th Cir. 1974) (promise to refrain from instituting a legal action held sufficient consideration for the issuance of a note deemed a security); *Rekant v. Desser*, 425 F.2d 872 (5th Cir. 1970) (land constituted consideration for a promissory note which qualified as a security).

¹⁰⁹ The common enterprise element is discussed in *Hammett*, *supra* note 12, at 65-70.

¹¹⁰ In contrast to the *Howey* Court, 328 U.S. 293 (1946), the Supreme Court in *United Hous. Found., Inc. v. Forman*, 421 U.S. 837 (1975), did not state that the benefit must be derived solely from the efforts of third parties. Thus, it now appears that the test is satisfied if the benefits are generated substantially by the efforts of others. Compare *United Hous. Found., Inc. v. Forman*, 421 U.S. 837, 852 n.16 (1975), with *SEC v. W.J. Howey Co.*, 328 U.S. 293, 298-99 (1946). Supporting this reading of *Forman* is the fact that the sole requirement has been abandoned by many lower courts. See, e.g., *SEC v. Glenn W. Turner Enterprises*, 474 F.2d 476 (9th Cir.), cert. denied, 414 U.S. 821 (1973) (pyramid investment scheme whereby efforts of the investors themselves affected amount of profits received held an investment contract).

¹¹¹ The Supreme Court's holding in *Forman* was based in part upon a finding that a purchaser's primary motivation in acquiring shares of stock in a public cooperative development is the acquisition of adequate low-cost housing and not the expectation of a benefit. 421 U.S. at 851. Similarly, the Second Circuit in *Grenader v. Spitz*, 537 F.2d 612 (2d Cir.), cert. denied, 429 U.S. 1009 (1976), held that shares in a privately-owned cooperative development did not constitute securities, emphasizing that the purchasers of the cooperative apartments were primarily interested in obtaining residences and that any profit motives were merely incidental. For a discussion of the *Grenader* decision, see Note, *Shares in Private Cooperative Apartment Held Not to Be Securities*, 51 ST. JOHN'S L. REV. 428 (1977).

vestment or commercial is imprecise and should be avoided. Bank loans, for instance, should not be characterized immediately as commercial without further scrutiny;¹¹² instead, these transactions must be individually analyzed and all circumstances surrounding each exchange carefully examined.¹¹³ It is submitted that the major concern in each case ultimately must be whether the legislature intended to provide a particular claimant with a federal remedy. Any facet of the transaction which may aid in the resolution of this question certainly should be included in the analysis.

CONCLUSION

Given the need for uniformity and flexibility, it would seem that an overly rigid test for determining the applicability of the 1933 and 1934 Acts to cases involving the transfer of promissory notes is neither mandated nor desirable. While an examination of the legislative history of both Acts appears to reveal that only investment instruments were intended to be subject to the provisions of the securities law, the absence of legislative guidance with respect to the definition of an investment transaction has led to difficulty in implementing this policy. Moreover, the failure of the federal courts to develop a uniform approach in this area has impaired the practitioner's ability to predict whether a particular promissory note will be treated as a security.¹¹⁴

¹¹² In the Fifth Circuit, bank loans have been held to be commercial transactions not subject to the operation of the securities acts. See *McClure v. First Nat'l Bank*, 497 F.2d 490 (5th Cir. 1974), *cert. denied*, 420 U.S. 930 (1975). Such an inflexible approach may lead to clearly improper results. See, e.g., *Bellah v. First Nat'l Bank*, 495 F.2d 1109 (5th Cir. 1974). In *Bellah*, the plaintiffs had borrowed money from the defendant bank for the purpose of developing an existing livestock business. The court dismissed the Bellahs' complaint, which alleged material misrepresentations by the bank in the loan agreement, on the ground that the notes were not securities. Although evidence existed that the Bellahs and the bank were engaged in a common enterprise characteristic of a security transaction, according to one commentator the court "felt compelled to view commercial loans as nonsecurity transactions to avoid subjecting commercial paper to the registration provisions of the 1933 Act." Comment, *The Status of Promissory Notes Under the Federal Securities Laws*, 1975 ARIZ. ST. L.J. 175, 187.

¹¹³ Legal analysts should consider other proposed definitions of the term security and should not limit their inquiry only to factors herein examined. Thus, the Uniform Commercial Code definition of a security may be useful in determining whether a particular promissory note is a security. Under the Code, *unless the context otherwise requires*, a security is any instrument issued in bearer or registered form which is of a type commonly recognized as traded in securities markets or exchanges or any medium for investment, and which is one of a class or series or else is divisible by its terms into a class or series of instruments and which evidences a share, participation or interest in an enterprise or an obligation of the issuer. See U.C.C. § 8-102 (1972 version) (emphasis added).

¹¹⁴ Much litigation continues to address the troublesome issue of the status of promissory

To remedy this problem, it is suggested that the federal courts adopt the method proposed herein for use in distinguishing investment from commercial transactions and place no arbitrary limitation upon the factors which may be considered. Such an approach would provide the necessary flexibility as well as assure that all courts would be considering the same criteria in making their determinations, namely all the elements of the transaction in question. Until an all-inclusive standard is utilized by the courts, flexibility and uniformity will not be achieved and litigants will be faced with unpredictable application of the 1933 and 1934 Acts.

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notes as securities. See, e.g., *Oliver v. Bostetter*, 426 F. Supp. 1082 (D. Md. 1977); *Lincoln Nat'l Bank v. Lampe*, [1976-1977 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 95,637 (N.D. Ill. 1976) (mem.); *Tri-County State Bank v. Hertz*, 418 F. Supp. 332 (N.D. Pa. 1976); *Fund of Funds, Ltd. v. Vesco*, [1976-1977 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 95,644 (S.D.N.Y. 1976). In the *Lincoln Nat'l Bank* and *Tri-County State Bank* decisions, the commercial-investment standard was applied to promissory notes given in exchange for bank loans, with both courts concluding that the notes in question were not securities. In contrast, the *Oliver* court stated that a note is a security within the meaning of the 1933 and 1934 Acts if it meets the *Howey* test for determining whether an investment contract is a security. 426 F. Supp. at 1085-86. Despite its finding that the plaintiffs did expect a profit, i.e., interest on the note, the *Oliver* court held that the notes, which were received by the plaintiffs in exchange for certain shares of stock, did not constitute securities. In view of the fact that "[b]y the sale of their stock to the defendant in exchange for the latter's note, plaintiffs sought to *terminate* their investment . . . , [they] were not 'investing' in any sense of the word . . . [but] were seeking to take their money *out of* the common enterprise." *Id.* at 1087 (emphasis in original). In light of these recent decisions, it is submitted, the need for a uniform, all-inclusive standard is manifest.